

CALL NO.

CA20N

CC

-Z 314

GOVT

facts
about
franchising



Ministry of
Consumer and
Commercial
Relations
Ontario




CA 20N
CC
- Z314 (10)

facts about franchising



Ontario

Ministry of
Consumer and
Commercial
Relations



Digitized by the Internet Archive
in 2022 with funding from
University of Toronto

What is franchising?

CH28 X

CC

- 2 314

Franchising is a method of operation used by companies to distribute products or services. The company (the franchisor) grants to the operator (the franchisee) the right to sell a product or service and to operate a business along the lines developed by the franchisor and using the franchisor's trade name or other designation.

Ideally, it is a continuing and supportive relationship between the parties to work for the benefit of both. But there are degrees of relationship and of success.

The right or privilege granted is called the franchise and it may include the right to sell the parent company's products, use its name, adopt its methods or use its symbols and trademarks. It may include only some of these rights.

Territory of operations may or may not be exclusive, and support may or may not be set up on a continuing basis.

Methods of operation

Some franchisors do virtually all the initial work of starting a new operation. They buy or lease the land and supervise construction of the building which has already been designed to their specifications. They install the equipment and fixtures, arrange the advance publicity and advertising and train the staff.

Some franchisors offer continuing support, from regular meetings and suggestions to newsletters and local advertising. A few leave you with all of the responsibilities and no help or advice.

These responsibilities may include payment of a royalty fee based on gross sales or maintaining a particular level of sales or they may include requiring you to attend training sessions, to purchase all equipment and supplies from the franchisor, or to maintain detailed financial records accessible to the franchisor.

The franchisor, in turn, is responsible for those items stipulated in the contract. If it isn't clearly and specifically stated in writing, don't assume that the franchisor will take care of it.

Why do some companies offer franchises?

There are many advantages to the franchisor. It's not his or her money but yours which is used to organize and operate the outlet; the franchisor collects a fee for the right to let you do business and usually a continuing royalty, as well as rental income from the property. Many of the potential problems, such as zoning or labor problems and inventory controls, are the responsibility of the franchisee.

By offering franchises, many companies broaden their marketing and economic base with little capital of their own.

Advantages and disadvantages of franchising

What you get will depend on the experience and integrity as well as the business and financial expertise of the franchisor. Advantages are few if you are purchasing a piece of paper permitting you to do business in a specified area. Your *only* advantages are what the franchisor provides for you and they may or may not include:

- the experience and know-how of the franchisor who has operated many outlets and has a background of successes.
- training of the franchisee and staff.
- a continuing source of information to the franchisee.
- a tradename or symbol which is well known and accepted by the buying public.

For every advantage there is a disadvantage which must be weighed carefully. Many franchisors collect a fee for the franchise and provide no further help. Even if support is provided, there may be disadvantages:

- services provided by the franchisor cost money and sometimes could be purchased more cheaply elsewhere.
- some of these services may not be of any value to the franchisee.
- many franchisors promise continuing support but fail to live up to that promise.
- if the franchisor operates from another jurisdiction and obligations are not fulfilled, it can be difficult to achieve redress. However, a form of redress is

available. Contract law prevails in the purchase of the franchise. Court action may be sought by a franchisee dissatisfied with a franchisor's action.

- in some franchises, there is no room for flexibility of operation.
- tradenames and symbols may not bring in as much business as hoped.
- misleading promises by franchisors could mean loss of your investment.
- franchisors could “oversaturate” the market.

Soliciting new franchisees

Franchisors use many methods to attract new franchisees. Classified and display advertising in magazines and newspapers, direct mailing lists and brochures at franchise locations are frequently-used procedures.

Some franchisors hold “exhibitions” in hotels and entice prospects to hear their sales pitch and sign up on the spot. No matter how good these opportunities sound, beware. *Never* sign anything, and that includes a cheque, without thoroughly investigating what you are buying.

One suggested practice is to check with other franchisees, in various parts of the community, to better understand day-to-day operations. Also, it is strongly advised to retain independent legal counsel, representing your personal interests.

Many franchisors offer sound opportunities for the careful investor and provide necessary support and advice. A lot of dissatisfaction between the two parties can stem from a misunderstanding of the terms of the agreement.

Purchasing a dream

Many people dream of owning a business and franchising may seem an easy way to do it. It's not. There is no easy way.

People who have bought franchises are often disillusioned; the profit projections predicted by the franchisor may be woefully inflated. It may take years of hard work before the business flourishes or it may never flourish.

Some franchisees feel “straitjacketed” by restrictions on products, architecture, innovations or methods of operation imposed on them by the parent company.

Costs of franchising

These vary from company to company. Be sure that *all* costs are clearly stated in the contract. There may be:

- a franchise fee
- continuing royalty fees
- rental or leasing costs
- advertising assessment fees
- costs of buying or leasing equipment
- cost of products supplied.

Some questions to ask before you invest

Variations in the franchising method make it a complex problem for the potential franchisee. Your investigation of the franchisor, the product, the territory, the contract and the existing outlets must be thorough. To do this, you'll need a lawyer and an accountant, both of whom should be experienced in dealing with franchises. Take all materials, contracts and proposals to them *before* you sign. Remember that responsible business people will give you the background information you require. Don't be hurried into signing a contract.

It is often difficult to solve misunderstandings or problems with a company which is operating from another jurisdiction. If you don't receive goods or services contracted for, it will be time-consuming and costly to sue a foreign franchisor.

Talk with the Canadian Association of Franchisors, the provincial ministries of consumer and commercial relations and industry, trade and technology (small business advice and counsel section) or your local chamber of commerce about the company's reputation and that of the product. These agencies make available information packages for potential franchisees. Also, most bookstores and libraries stock a selection of how-to books on franchising. Get the answers to the following questions.

The franchisor:

- Is the company financially stable? How does it make its money? (Money should come from successful franchises and products, not reselling unprofitable franchises.)

- If a subsidiary, who is the parent company?
- How long has the company been in business?
- How long has the present management been with the company?
- Does the company franchise other products or services?
- Would those products be in competition with your franchise?
- On what facts is the profit projection based?
- Will the reputation and credit record of the franchisor help you to obtain the necessary financial backing to purchase a franchise?
- How many franchises are in operation?
- Are there immediate plans for further expansion in your area?
- Where will new franchises be located?
- Is there a useful training program?
- Is it paid for by the company?
- What continuing assistance is provided? Ask for specifics.
- Does the franchisor help recruit and train staff on a continuing basis?
- Will you receive help in selecting and purchasing a location? Will they charge for a marketing study?
- Does the franchisor offer financial assistance in purchasing the franchise? At what rate?
- Who pays for initial opening costs, displays and layouts, local and national advertising?
- Are there new methods or innovations since the franchisor first started?
- Is a manual of operation provided?
- Is the price of the franchise variable? How?

The product or service

- Is there a demand for it?
- How long has it been on the market?
- Is it seasonal? Is it a luxury? Is it a fad?
- Can it be successfully marketed in this area?
- Can you buy similar products in this area? At what price?
- What guarantee do you have that the franchisor will be able to continue getting the product for you at a fair price?
- What product warranties or guarantees are there?
- Who backs them, repairs them and pays for repairs?
- How many people in the area are potential customers?

- Is it protected by a trademark or copyright? Is it patented?

The territory

- Is it exclusive? What guarantee do you have?
- Is it clearly-defined geographically or only by population?
- Is the population increasing or decreasing?
- Are there proposed changes in traffic patterns or redevelopment which could affect the business in the proposed location? (Check municipal offices about local by-laws.)
- What competition is in the area? How are other businesses doing?
- How expensive are taxes and insurance in the area?

The contract

- Does it state the duration and renewal of the agreement and all costs to you?
- Is there a renewal fee?
- Must you purchase a minimum amount of merchandise per year?
- What other payments must you make?
- Is there a royalty payment? Is it reasonable?
- Is there a sales quota? Does the company have the right to terminate the contract if the quota isn't met?
- Under what other terms can the franchisor terminate the franchise?
- Is there provision for repurchasing equipment and inventory? How would the price be determined?
- Do you have the right to resell, renew or reassign the franchise?
- Under what conditions?
- Under what conditions can you terminate the franchise?
- Does your family have the right to continue the operation if you die? Under what conditions?
- Do you have renewal options for both the contract and the lease of the building? Do they expire concurrently?
- Has the franchisor the right to repurchase the franchise? At what price?
- Do you have the right to all innovations and new products offered by the franchisor?
- Is there a procedure for settling disputes?
- Must you purchase all equipment and supplies from the franchisor?
- Must you restrict your business to only the franchisor's products or services?

The franchisee

Talking to the operators of existing franchises will be helpful in determining the reliability of the franchisor and the profitability of the product.

- What was the total cost of the franchise?
- What were the hidden or unexpected costs?
- Is there a continuing fee? Is it reasonable?
- If there is a minimum quota, is it difficult to achieve? How long was the franchisee in operation before the business became profitable?
- Are products and equipment supplied by the franchisor satisfactory and delivered promptly?
- Was the training program adequate? Were staff members also trained?
- Was the profit projection accurate?
- How are disagreements with the franchisor handled?
- Is this arrangement workable?
- What reports to the company are necessary?
- Is the marketing promotional and advertising assistance provided by the company satisfactory to the franchisee?
- What problems have been encountered?
- What changes should be made in the existing contract?

Pitfalls and problems

The most frequent complaint of franchisees is that they were led to expect a certain profit which just didn't happen. Usually potential franchisees have unrealistic expectations: they want to hear how much money they are going to make and reality is a shock. Another problem is a lack of sufficient help and advice from the franchisor. Too often there is no one to turn to when the new franchisee runs into trouble.

Protection for the franchisee

When you sign a franchise agreement you are entering a business contract. A lawyer and an accountant who understand the franchising method can help you spot potential problems and avoid them. They can show you what changes should be made to the existing contract to protect your rights and help you to become successful in this venture.

Insist that the franchisor hold your franchise deposit in trust until your franchise outlet is open and operating. Reliable business persons will agree to this provision, which is particularly important if the product or service is not yet marketed and company stability is in doubt.

But the best protection is you.

Don't sign anything in a hurry.

Do investigate the franchisor's credit record and reputation.

Do take the contract to a lawyer and accountant.

Do ask the advice of your bank manager.

Do make sure that the territory is clearly-defined and not already saturated.

Consumer Services Bureaus

Toronto

2nd Floor
555 Yonge St.
Toronto, Ontario
M7A 2H6
(416) 963-0321

London

P.O. Box 5600
Postal Station "A"
Main Floor
80 Dundas St.
London, Ontario
N6A 2P3
(519) 679-7150

Peterborough

139 George St. N.
Peterborough, Ontario
K9J 3G6
(705) 743-8728

Thunder Bay

P.O. Box 5000
1st Floor
435 James St. S.
Thunder Bay, Ontario
P7C 5G6
(807) 475-1641

Hamilton

P.O. Box 2112
5th Floor
Ontario Govt. Bldg.
119 King St. W.
Hamilton, Ontario
L8N 3Z9
(416) 521-7554

Ottawa

2nd Floor
10 Rideau St.
Ottawa, Ontario
K1N 9J1
(613) 566-3878

Sudbury

5th Floor
199 Larch St.
Sudbury, Ontario
P3E 5P9
(705) 675-4378

Windsor

Suite 627
250 Windsor Ave.
Windsor, Ontario
N9A 6V9
(519) 254-6413

We'd like to hear from you.

The consumer ministry welcomes any comments and suggestions on its information materials or programs. In this way, we can best respond to your needs in the marketplace.

Please address your comments to:

Communications Branch
Ministry of Consumer and
Commercial Relations
9th Floor
555 Yonge St.
Toronto, Ontario
M7A 2H6

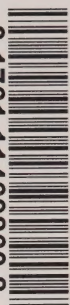


Ontario

Ministry of
Consumer and
Commercial
Relations

REPR. 03/89-10M

ISBN 0-7729-3788-5



3 1761 11469860 8